## Re: PERSONAL - IS THIS WRONG? [UNCLASSIFIED] [Non-Record]

Tucker, Paul

Sent: 30 October 2008 13:32

To: jheywood:

Will be sure to call later

---- Original Message -----From: Jeremy Heywood

To: Tucker, Paul

Sent: Thu Oct 30 13:15:51 2008

Subject: RE: PERSONAL - IS THIS WRONG? [UNCLASSIFIED] [Non-Record]

WOuld welcome a conversation on this at some point - plus a more general update

----Original Message----From: Jeremy Heywood Sent: 28 October 2008 16:08

To: 'Tucker, Paul'

Subject: PERSONAL - IS THIS WRONG? [UNCLASSIFIED] [Non-Record]

There is a continued lack of short term money in the system. Although the BoE is offering a considerable supply of liquidity, the various facilities need eligible collateral. It is likely that the bank's have either insufficient eligible collateral to make full use of the facilities or that the collateral that would qualify has not yet been identified and used due to operational complexities.

The BoE's latest Long Term Repo (LTR) operation on 21st Oct offered £30bn of three month loans. Only £7.67 was taken up, at an average yield of 4.27%. This is despite GBP LIBOR being at 6.08% on the day. Given that use of the LTR carries no stigma and that funding remains in demand, the likely explanation is that the banks had insufficient collateral ready to make full use of the facility. An alternative explanation is that banks remain rejudicant to lend funds seems unlikely, given that borrowing is happening in the interbank market at much higher rates (including when that borrowing is Government guaranteed).

The BoE could temporarily widen eligible collateral still further, to include bank paper; senior debt and certificates of deposit. The subscribing bank would be required to use paper other than its own, thus requiring a dual default from the subscribing and issuing bank before the BoE were exposed to loss. The BoE Consultative Paper "The Development of the Bank of England's Open Market Operations" October 2008 argued against allowing bank arguing that such actions would, in effect, be lending to the banking system secured against a claim on the banking system. However, the ECB and the Federal Reserve have both allowed bank securities as eligible collateral. (Sterling Libor has been stickler than \$ and less so E libor)

The BoE could temporarily allow bank collateral at both the Discount Window and in the LTR's, but not in the longer term Special Liquidity Scheme. This would keep operational flexibility to withdraw the measure quickly, as liquidity conditions stabilise and the BoE wishes to both withdraw the monetary stimulus and reduce its exposure to the banking system as a whole

----- Original Message-----From: Tucker, Paul Sent: 26 October 2008 11:11

To: Jeremy Heywood

Subject: Re: Manythanks for fitting in supper [UNCLASSIFIED] [Non-Record]

In about an hour?

--- Original Missage --From: Jeremy Heysteod To: Tucker, Paul; Scholar, Tom Seni: Sun Oct 15 14:00:58 2008 Subject: LIBOR

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Comment from UBS (in confidence - pi protect) in case you have not had this directly. Keen to discuss this general issue with you next week unless LIBOR does start to fall fairly sharply

in summary Liboris decline is in train but it will be gradual. To speed it up a change in the quarantee fee (to bring it in fine with the Clutch scheme) is called for, I am an advocate for speeding it up.

I month Starting Liber is the rate at which AA nated banks can boundwifern one another. This is an unsequed befrowing rise, Liber is "fixed" at 10:30 am by everaging across quotes submitted by a partial of the parting banks. In the last 2 weeks the market has noticed that both Bardays and RBS have bid, Ater the 1030 fixing, at levels up to 5 pp above the fixing submitted by a parting banks. In the last 2 weeks the market has noticed that both Bardays and RBS have bid, Are the 10:30 and Bardays conditioned to bid for cash at the higher fitting the first parting the rest of the day. Brokens report that when the Bank of England out rates on the 4th October by 500ps at 12 noon Bardays conditioned to bid for cash at the higher fitting that they are prepared to borrow 10:30 am level. The market has been approximating over what these two banks might be doing and have interpreted these adone as a deliverate signal that they are prepared to borrow unaccurred at 5.00%.

There is no incentive for lenders to offer funds after 10:30 at or below Libor when they know two banks will continue to pay chars Libor throughout the remainder of the day.

For example, on 23rd October 3 month Liber fixed at 8,005%. RBS continued to laid 6,050% through the remainder of the day.

Why might Buckys and RBS behave like this? We believe it is because Liber benowing is chesper than any alternative, including the GBS. Serdays could issue a 3 month CD within the GBS at Liber less 100, at best (maybe Liber less 505ps), UBS estimates Berclays GBS quarantee (se is 124 bps (12 nonth median CDS plus 505ps) which gives an all in CGS at Liber less 100, at best (maybe Liber less 505ps), UBS estimates Berclays GBS quarantee (se is 124 bps (12 nonth median CDS) in CGS signals that banks using the hierbank market cost of Uborn24 at best, i.e. significantly more than Ubor borrowing WHATEVER level Liber times at. Additionally, avoiding the CGS signals that banks using the hierbank market need no government assistance in borrowing.

Although Liber has fallen by 30 bps since the announcement of the Quarantee Scheme, the size of the fall has been impacted by the implementation. We view the Liber market as dividing between 2 borrowers (HBOS, RBS and Saudays) and two lenders (Libyds and HBGO). The borrowers do not have a cheaper sizement exchange the stand off. Index more cheapty. There is no immediately apparent machanism to change this stand off.

if the CGS (seehed not included the 50 bps it would have produced a different dynamic. For example, Burdays could have leaded at the money market would have known this. In this gase Liber by county and in cost of Liber less 28. In this case Liber by cowing would have been the second heat option and the landes in the money market would have known this. In this case Liber by county and in cost of Liber less 28. In this case Liber by would have been the second heat option and the landes in the money market would be 5.00% (or Bank Rate plus 60bps). example the level of Liber less 100bps would probably have failen to where 3 month Treasury Biffs are reading (4,00%) and therefore Liber less 100bps would be 5.00% (or Bank Rate plus 60bps). Furthermore, edditional Bank Rate cuts would push TBIII yields lower and therefore Liber loo, rather than having Liber sket at 6.00%.

Another expect of the current CQS fee structure is that reductions in GDS do not feed into lower fees while the September sumoli keeps the fee high. If the averaging window was more currently chosen and the fee reduced as GDS fell it might be possible to create a virtuous downward cycle in Ubor.

For example, the Dutch who had the benefit of time to study the UK sokeme chose different fees for short and long termborrowing. For less than 1-year they charge 60bps flat and for longer than 1-year they charge median GDS plue 50bps but with the median window running from January 2007 to August 2006, excluding the Septembar turnoil.

If the UK followed the Outon example for the CDB window, the CGB (se would tell by between 20 and 80bps but the all in its would remain between 75bps and 1 tobps for the eight initial gardeparts. Bardays fee would be 26bps, HBO\$ 75bps and RB\$ \$5bps. While in theory the might give sub tites handing in practice the benefit would be 20rd without the bord without the conditions.

Our suggestion is that it would be batter to distriguish between short and long term use of the CGB and to charge a lower factor that ensures sub-Ubor funding at least until Ubor replaces. We suggest initiatly following the Dutch example and using Sobps since this can easily be justified on competition grounds but would keep the fee under review as the market the standard of the can easily be justified on competition grounds but would keep the fee under review as the market the standard of the can easily be justified on competition grounds but would be better to distriguish between short and long term use of the CGB and to charge a lower fact that ensures are the feet of the can easily be justified on competition grounds but would be sufficient to distriguish between short and long term use of the CGB and to charge a lower fact that ensures the can easily be justified on competition grounds but would be sufficient to distribute the can easily be justified on competition grounds but would be sufficient to the can easily be justified on competition grounds but would be considered to the can easily be justified as the can easily be

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#### TYPED-UP VERSION OF E-MAIL OF 26 OCTOBER 2008

\*\*\*\*\*Original Message\*\*\*\*\*

From: Jeremy Heywood

To: Tucker, Paul; Scholar, Tom Sent: Sun Oct 26 14:09:56 2008

Subject: LIBOR

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Comment from UBS (in confidence – pl protect) in case you have not had this directly. Keen to discuss this general issue with you next week unless LIBOR does start to fall fairly sharply

In summary Libor's decline is in train but it will be gradual. To speed it up a change in the guarantee fee (to bring it in line with the Dutch scheme) is called for. I am an advocate for speeding it up.

3 month Sterling Libor is the rate at which AA rated banks can borrow from one another. This is an unsecured borrowing rate. Libor is 'fixed' at 10:30am by averaging across quotes submitted by a panel of reporting banks. In the last 3 weeks the market has noticed that both Barclays and RBS have bid, after the 10:30 fixing, at levels up to 5bps above the fixing throughout the rest of the day. Brokers report that when the Bank of England cut rates on the 8<sup>th</sup> October by 50bps at 12 noon Barclays continued to bid for cash at the higher 10:30am level. The market has been speculating over what these two banks might be doing and have interpreted these actions as a deliberate signal that they are prepared to borrow unsecured at 6.00%.

There is no incentive for lenders to offer funds after 10:30 at or below Libor when they know two banks will continue to pay above Libor throughout the remainder for the day.

For example, on 23<sup>rd</sup> October 3 month Libor fixed at 6.005%. RBS continued to bid 6.050% through the remainder of the day.

Why might Barclays and RBS behave like this? We believe it is because Libor borrowing is cheaper than any alternative, including the CGS. Barclays could issue a 3 month CD within the CGS at Libor less 100, at best (maybe Libor less 50bps). UBS estimates Barclays CGS guarantee fee is 124 bps (12 month median CDS plus 50bps) which gives an all in CGS cost of Libor+24 at best, i.e. significantly more than Libor borrowing WHATEVER level Libor fixes at. Additionally, avoiding the CGS signals that banks using the Interbank market need no government assistance in borrowing.

Although Libor has fallen by 30bps since the announcement of the Guarantee Scheme, the size of the fall has been impeded by the implementation. We view the Libor market as dividing between 3 borrowers (HBOS, RBS and Barclays) and two lenders (Lloyds and HSBC). The borrowers do not have a cheaper alternative and lenders see no pressure to offer funds more cheaply. There is no immediately apparent mechanism to change this stand off.

If the CGS fee had not included the 50 bps it would have produced a different dynamic. For example, Barclays could have issued a 3 month CD at Libor less 100 plus a fee of 74bps giving an all in cost of Libor less 28. In this case Libor borrowing would have been the second best option and the lenders in the money market would have known this. In this example the level of Libor less 100bps would probably have fallen to where 3 month Treasury Bills are trading (4.00%) and therefore Libor would be 5.00% (or Bank Rate plus 50bps). Furthermore, additional Bank Rate cuts would push TBill yields lower and therefore Libor too, rather than having Libor stuck at 6.00%.

Another aspect of the current CGS fee structure is that reductions in CDS do not feed into lower fees while the September turmoil keeps the fee high. If the averaging window was more carefully chosen and the fee reduced as CDS fell it might be possible to create a virtuous downward cycle in Libor.

For example, the Dutch who had the benefit of time to study the UK scheme chose different fees for short and long term borrowing. For less that 1-year they charge 50bps flat and for longer than 1-year they charge median CDS plus 50bps but with the median window running from January 2007 to August 2008, excluding the September turmoil.

If the UK followed the Dutch example for the CDS window, the CGS fee would fall by between 20 and 80 bps but the all in fee would remain between 75bps and 110bps for the eight initial participants. Barclays fee would be 95bps, HBOS 75bps and RBS 85bps. While in theory this might give sub Libor funding in practice the benefit would be borderline.

Our suggestion is that it would be better to distinguish between short and long term use of the CGS and to charge a lower flat fee that ensures sub Libor funding at least until Libor reduces. We suggest initially following the Dutch example and using 50bps since this can easily be justified on competition grounds but would keep the fee under review as the market develops.

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# • RE: Manythanks for fitting in supper [UNCLASSIFIED] [Non-Record]

Jeremy Heywood

Sent: 25 October 2008 20:47

.To: Tucker, Paul

did u text me earlier?
when is a good time to talk>

### Re: Might be scuttle butt - are u hearing this rumour? [UNCLASSIFIED] [Non-Record]

Tucker, Paul

Sent: 22 October 2008 22:50

jheywood To:

Yep. Dollar spreads still above ours at 3 months. But I'm concerned too, for both parts of our mission

---- Original Message ----From: Jeremy Heywood

To: Tucker, Paul

Sent: Wed Oct 22 22:49:04 2008

Subject: RE: Might be scuttle butt - are u hearing this rumour? [UNCLASSIFIED] [Non-Record]

obviously we are v concerned that US rates are tumbling but we remain stuck!

----Original Message-----From: Tucker, Paul

Sent: 22 October 2008 22:17

To: Jeremy Heywood

Subject: Re: Might be scuttle butt - are u hearing this rumour?

[UNCLASSIFIED] [Non-Record]

I know. But I don't think that can be all of it. Cos I don't think they'd be an influence on euro libor, which has also been sticky. But we are trying to monitor what's going on. Big question may be about non bank financial Institutions

---- Original Message ----From: Jeremy Heywood To: Tucker, Paul Sent: Wed Oct 22 14:47:16 2008 Subject: Might be scuttle butt - are u hearing this rumour? [UNCLASSIFIED] [Non-Record]

没有流行的方式的自身作为为有利用公司产业再创目实在的有效企业的企业的企业的有利的企业的对方在而开发的实现的企业实 This email has reached the Bank via the Internet or an external network

From the money market trenches:

Sterling 3m Libor is high because Barclays are bidding it. They are bidding 2bps ABOVE Libor. This has been going on for three weeks. The day BoE cut 50 Barclays continued to bid the old level (as the rates had not been cut). A lot of speculation in the market over what they are up to.

# LIBOR spreads [RESTRICTED] [Record]

Jeremy Heywood

Sant: 22 October 2008 10:08

To: Tucker, Paul

any policy options we should be considering?

From: Tucker, Paul Sent: 21 October 2008 21:27

To: Jeremy Heywood Subject: Re: Manythanks for fitting in supper [UNCLASSIFIED]

[Non-Record]

Euro ones haven't fallen markedly either so far

Dollar ones were significantly higher

A handful of US banks have been lending fairly actively (that's a relative term)in dollars. I think (think) that may have something to do with the fact that a number of US money centre banks have been enjoying flight to quality flows, whereas (no doubt overstating it a bit) that's been true of only habe in sterling and one bank can't turn a whole market.

Hope that helps a bit

Paul

---- Original Message ---From: Jeremy Heywood
To: Tucker, Paul
Sent: Tue Oct 21 20:12:36 2008
Subject: RE: Manythanks for fitting in supper [UNCLASSIFIED]
[Non-Record]

Hope all well

Why are UK LIBOR spreads not failing as fast as US?

----Original Message----From: Tucker, Paul Sent: 13 October 2008 20:31 To: Jeremy Heywood

Subject: Re: Manythanks for fitting in supper

That's quite something coming from where you sit!

Let's hope it worksil

---- Original Message -----From: Jaremy Heywood

To: Tucker, Paul Sent: Mon Oct 13 19:14:07 2008

Subject: RE: Manythanks for fitting in supper

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What a few days!

----Original Message----From: Tucker, Paul Sent: 06 July 2008 12:51 To: Jeremy Heywood Subject: Manythanks for litting in supper

V good to see you

Best

Paul